

Message Text

CONFIDENTIAL

PAGE 01 STATE 169414

11

ORIGIN EB-03

INFO OCT-01 ISO-00 /004 R

66619

DRAFTED BY:EB /IFD/OMA:RJRYAN:DLS

APPROVED BY:EB/IFD/OMA:RJRYAN

----- 077070

R 041549Z AUG 75

FM SECSTATE WASHDC

TO AMEMBASSY BONN

C O N F I D E N T I A L STATE 169414

FOLLOWING REPEAT STATE 169414 ACTION LONDON 18 JUL 75

QUOTE

C O N F I D E N T I A L STATE 169414

E.O. 11652: GDS

TAGS: EFIN, ENRG

SUBJECT: OIL PRICE/OIL MONEY PROBLEM

FOR AMBASSADOR RICHARDSON FROM THE SECRETARY

1. I READ WITH INTEREST YOUR REPORT ON HAROLD LEVER'S VIEWS ON INDEXATION. THESE VIEWS ARE NOT, AS YOU NOTED, ENTIRELY NEW TO US, BUT BECAUSE THEY HAVE NOW BEEN PRESENTED IN SOME DETAIL, IT IS IMPORTANT THAT WE RESPOND MORE FULLY THAN WE HAVE TO DATE. I WOULD APPRECIATE IT, THEREFORE, IF YOU WOULD FOLLOW UP WITH LEVER, EXPLAINING THE REASONS WHY THE USG DOES NOT SHARE HIS ASSESSMENT, DRAWING ON THE POINTS SET OUT BELOW.

2. ONE OF THE BASIC PREMISES OF LEVER'S ARGUMENT IS THAT PRICE STABILITY AND BROADER FINANCIAL PROBLEMS ARE THE HEART OF ENERGY CRISIS. THIS IS NOT OUR ASSESSMENT. INDEXA-
CONFIDENTIAL

CONFIDENTIAL

PAGE 02 STATE 169414

TION, WHILE POSSIBLY PROVIDING SOME RELIEF TO OIL CONSUMERS

BY AFFORDING A MEASURE OF FUTURE PRICE STABILITY, LEAVES THE PRIMARY THREAT IMPLIED BY OUR CONTINUING DEPENDENCE ON OPEC OIL UNRESOLVED. THE MAJOR TASK FACING INDUSTRIALIZED OIL CONSUMERS IS HOW TO REDUCE OUR DEPENDENCE ON OPEC AND THUS OUR LONG-TERM VULNERABILITY TO OPEC PRESSURES. LEVER'S SOLUTION DOES NOT ADDRESS THIS PROBLEM: IT COULD IN FACT

WORSEN IT BY WEAKENING CONSUMER RESOLVE TO DEAL WITH UNDERLYING CAUSES OF PRESENT SITUATION.

3. I HAVE PUBLICLY EXPRESSED OUR WILLINGNESS TO CONSIDER INDEXATION OF OIL PRICES IN RETURN FOR A SUBSTANTIAL PRICE REDUCTION. HOWEVER, WE SEE NO SIGN THAT PRODUCERS ARE READY TO ACCEPT SUCH AN ARRANGEMENT. SINCE OPEC IS UNLIKELY TO ACCEPT INDEXATION SCHEME WHICH WOULD PERMIT OIL PRICE TO FALL, THIS WOULD SHIFT RISK NORMALLY SHARED BY BOTH OIL PRODUCERS AND CONSUMERS ONTO LATTER ALONE. EVEN IF OPEC WERE TO AGREE TO A PRICE REDUCTION, WE WOULD HAVE TO CONSIDER THE VERY SERIOUS INFLATIONARY IMPACT WHICH OIL PRICE INDEXATION WOULD HAVE. THE EXPECTATION OF HIGHER PRICES WOULD BUILD-IN INFLATIONARY PRESSURES. MORE IMPORTANT, HOWEVER, IS PROBLEM POSED BY DEMANDS FOR EQUAL TREATMENT FOR OTHER COMMODITIES ONCE PRINCIPLE OF INDEXATION HAS BEEN ACCEPTED FOR OIL. INDEXATION OF OTHER COMMODITIES WOULD THEN FEED BACK TO OIL PRICES, THUS CREATING AN INFLATIONARY SPIRAL. SINCE INDEXATION OF COMMODITIES WOULD REMOVE THEIR PRICES FROM MARKET INFLUENCES, WIDE EXCESSES OR SHORTFALLS IN PRODUCTION COULD CONCUR.

4. OUR LACK OF ENTHUSIASM FOR LEVER'S PROPOSALS ALSO STEMS FROM A DIFFERENT PERCEPTION OF OPEC'S MARKET LEVERAGE. WE BELIEVE THAT THERE ARE ECONOMIC AND POLITICAL CONSTRAINTS ON OPEC'S ABILITY FURTHER TO INCREASE OIL PRICES DRAMATICALLY EVEN IN THE SHORT RUN. OVER TIME, IEA EFFORTS TO REDUCE DEPENDENCY ON IMPORTED OIL SHOULD STRENGTHEN OUR BARGAINING HAND IN DEALING WITH OPEC. AN INDEXATION SCHEME CONCLUDED WITH ALL OPEC PRODUCERS WOULD ELIMINATE ANY POSSIBILITIES WE MAY HAVE OF PLAYING SOME OFF AGAINST OTHERS. AS AMBITIOUS DEVELOPMENT PROGRAMS IN

CONFIDENTIAL

PAGE 03 STATE 169414

CERTAIN PRODUCERS BEGIN TO RESULT IN LEVELING OFF OR DECLINE IN CURRENT INCOME SURPLUS, SOME OF THEM MAY BECOME MORE INCLINED THAN AT PRESENT TO FIND WAYS TO INCREASE THEIR OUTPUT AT THE EXPENSE OF OTHERS.

5. WE HAVE ALSO INDICATED THAT WE ARE WILLING TO DISCUSS THE TREATMENT OF ENERGY-RELATED FINANCIAL PROBLEMS IN THE CONTEXT OF PRODUCER-CONSUMER DISCUSSIONS. WE COULD HAVE

GREAT PROBLEMS, HOWEVER, WITH LEVER'S PROPOSAL FOR SPECIAL TREATMENT FOR OIL PRODUCERS' FINANCIAL ASSETS. BY ASSURING OPEC ABOVE-NORMAL RETURNS ON THEIR INVESTMENTS WE WOULD BE ADDING TO THE PRESENT AND FUTURE BURDEN OF HIGHER OIL PRICES. THERE SEEMS TO BE NO NEED FOR INDUSTRIAL COUNTRIES TO CREATE SPECIAL INVESTMENT OUTLETS, OR ESPECIALLY FAVORABLE TYPES OF ASSETS, FOR OPEC COUNTRIES.

WE WOULD RATHER ARGUE THAT PRIVATE MARKETS, AUGMENTED BY SPECIAL RECYCLING FACILITIES AND MEASURES TO HELP LDCS, HAVE PROVED CAPABLE OF MANAGING OPEC FINANCIAL SURPLUSES. OUR NEED FOR THE ORDERLY HANDLING OF OPEC FUNDS IS MATCHED BY THEIR NEED FOR MARKETS IN WHICH THEY CAN INVEST. THERE ARE SIMPLY NO OTHER MAJOR CAPITAL MARKETS INTO WHICH THESE FUNDS CAN GO. THE INEVITABLE BUILD-UP OF PRODUCER ASSETS IN INDUSTRIALIZED COUNTRIES PROVIDES AN INCENTIVE FOR PRODUCERS TO CONTINUE TO INVEST RESPONSIBLY. ALTHOUGH IT IS NOT CLEAR THAT LEVER IS PROPOSING CONSOLIDATION OF OIL PRODUCER INVESTMENTS INTO AN INTERNATIONAL INVESTMENT POOL, SUCH A STEP COULD ACTUALLY INCREASE THE COLLECTIVE DISRUPTIVE POWER OF THE MANIPULATION OF THESE FUNDS.

6. SPECIAL TREATMENT OF OPEC FUNDS WOULD ALSO POSE POLITICAL DIFFICULTIES SINCE DOMESTIC INVESTORS AND CONSUMERS ARE NOT GIVEN SUCH PROTECTION. IN ADDITION, WE WOULD HAVE DIFFICULTY ACCORDING A GUARANTEED STATUS FOR FUNDS GENERATED AT LEAST IN PART FROM US INVESTMENTS WHICH HAVE BEEN EXPROPRIATED OR TAKEN BY OPEC GOVERNMENTS.

7. WE ALSO DO NOT SHARE LEVER'S CONFIDENCE THAT OPEC WOULD ADHERE TO THE DEAL HE PROPOSES, E.G. AN AGREEMENT AMONG GOVERNMENTS. THE TEHRAN PRICE AGREEMENT OF 1971 WAS VIOLATED BY PRICE RISE OF 1973, ALTHOUGH IRAN, SAUDI
CONFIDENTIAL

CONFIDENTIAL

PAGE 04 STATE 169414

ARABIA, AND KUWAIT HAD ASSURED THE US GOVERNMENT THAT THEY WOULD FULLY RESPECT THE AGREEMENT. THE OIL EMBARGO OF 1973 WAS INCONSISTENT WITH TREATY OBLIGATIONS OF 3 OPEC STATES. ARAB OIL EXPORTERS THUS HAVE CLEARLY DEMONSTRATED THEIR WILLINGNESS -- WHEN THEY CONSIDER THE ISSUE IMPORTANT ENOUGH -- TO ACT IN WAYS CONTRARY TO THEIR INTERNATIONAL LEGAL OBLIGATIONS AND TO SUBORDINATE ECONOMIC INTERESTS TO POLITICAL AIMS. ATTEMPTS TO SWEETEN THE AGREEMENT TO SATISFY FUTURE PRODUCER ASPIRATIONS COULD BOTH WHET THEIR APPETITE AND STRENGTHEN THEIR HAND IN FUTURE NEGOTIATIONS.

8. IT IS UNAVOIDABLE THAT THE SUBJECT OF INDEXATION -- BOTH OF OIL PRICES AND OF INVESTMENTS -- WILL BE RAISED IN COMING PRODUCER/CONSUMER DISCUSSIONS. WE WOULD HOPE THAT WE COULD CONTINUE THE CANDID DISCUSSION OF THESE

ISSUES WITH HMG AND WITH LEVER.

9. WE WOULD ALSO APPRECIATE LEARNING EXTENT TO WHICH
LEVER'S VIEWS WERE DISCUSSED AT EC SUMMIT AND HAVING YOUR
VIEW OF DEGREE TO WHICH LEVER'S POSITION IS COLORED BY HIS
PERCEPTION OF UNIQUE PROBLEMS FACING THE U.K. DOES HE SEE
THE U.K. IN SHORT RUN EXTREMELY VULNERABLE TO ANOTHER
ROUND OF SUBSTANTIAL OIL PRICE INCREASES? IS HIS ARGUMENT

FOR INDEXATION A STOP-GAP MEASURE UNTIL NORTH SEA OIL
BRINGS SELF-SUFFICIENCY? IS THERE ANY INDICATION OTHERS
WITHIN THE U.K. GOVERNMENT, INCLUDING PRIME MINISTER
WILSON, ARE BEING PERSUADED BY LEVER'S ARGUMENT? KISSINGER
UQTE INGERSOLL

CONFIDENTIAL

NNN

Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: n/a
Control Number: n/a
Copy: SINGLE
Draft Date: 04 AUG 1975
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: greeneet
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1975STATE169414
Document Source: CORE
Document Unique ID: 00
Drafter: EB /IFD/OMA:RJRYAN:DLS
Enclosure: n/a
Executive Order: RR
Errors: N/A
Film Number: n/a
From: SECSTATE WASHDC
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1975/newtext/t19750882/aaaacupy.tel
Line Count: 183
Locator: TEXT ON-LINE
Office: ORIGIN EB
Original Classification: CONFIDENTIAL
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 4
Previous Channel Indicators: n/a
Previous Classification: CONFIDENTIAL
Previous Handling Restrictions: n/a
Reference: n/a
Review Action: RELEASED, APPROVED
Review Authority: greeneet
Review Comment: n/a
Review Content Flags:
Review Date: 02 JUN 2003
Review Event:
Review Exemptions: n/a
Review History: RELEASED <02 JUN 2003 by CunninFX>; APPROVED <07 OCT 2003 by greeneet>
Review Markings:

Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
06 JUL 2006

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: OIL PRICE/OIL MONEY PROBLEM
TAGS: EFIN, ENRG
To: BONN
Type: TE
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 06 JUL 2006